24 February 1948

MEMORANDUM FOR MR. HAWKINS:

Subject: Bosch Patent Question.

Your memorandum to me of 20 February concerning the Bosch patent question indicates that you will approve royalty-free licenses on existing patents and inventions but are inclined to favor a "reasonable royalty" for patents and investions conceived after the date of the decree.

If the question is not closed I would like to present some additional facts for your consideration. This seems important to us in view of our belief that Bosch, to a great extent, attained its power through its patent position and that unless Bosch is compelled to share its research with the newly created competitors they will be placed at a serious disadvantage.

I did not intend in my memo of 20 February to rest our whole position on decisions in Antitrust cases. You suggested that we look into the DuPont case. We then followed the line of decision down, and pointed out the position of the Department of Justice in the Shoe Machinery case. However, there is much more back of the Department of Justice's position in the Shoe Machinery complaint than the decisions in Hartford Empire and National Lead. Before adopting a policy in Germany I think it might be worthwhile to review some of that background.

You said that the adoption of our proposal to give newly created competitors free access to Bosch's research and inventions for five years would remove the incentive for Bosch to do research and would encourage new firms to lean on Bosch.

That has not proved to be the case in the automobile industry in the United States. Members of that industry, one of the most efficient in the world, have participated for 33 years in voluntary arrangements whereby each grants royalty-free licenses to all applicants.

Mr. Alfred Reeves, Vice President and General Manager of the Automobile Manufacturers Association, New York, in testimony before the Temporary National Economic Committee, gave the history and main characteristics of the cross-licensing system administered by the Association. He stated that the first agreement was entered into on January 1, 1915, by 61 manufacturers of automobiles and trucks who contributed 547 patents to the original "pool", the contributions ranging from 0 to 110 patents. His explanation of the formulation of the agreement was as follows:

> "Well, I think it came partially from the situation in the Selden case /a patent infringement case affecting the automobile industry/, the manufacturers were having

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great difficulty getting out production; they didn't want to be bothered with patents; they didn't want to sue one another. They had had enough concern over the Selden case itself, and there seemed to be a need for keeping patents out of the situation and trying to develop as good cars as they could produce at prices at which the public could buy because at that time most of the cars were very high priced cars."

The effect of the agreement was to give each manufacturer who was a party thereto royalty-free licenses under patents of all of the manufacturers who were parties to the agreement. The agreement applied not only to the 547 existing patents but also to all patents which might be acquired by any of them during the term of the agreement (ten years) except patents on inventions of a revolutionary character. During the ten-year period, no patents came under the exception. The 1915 agreement was renewed in 1925, 1930 and 1935, but with some modifications. When asked to state his opinion as to the general effect that the cross-licensing agreement had on the automobile industry in terms of productivity and price in the period between 1914 and 1925, Mr. Reeves replied as follows:

"I think it is generally agreed that it tended to throw the automobile industry open to broad competition with rewards going to the companies that made the best product, sold at the lowest price, but with an opportunity to every company to make a car based on the best that the art know about at the time."

When asked to indicate whether the agreement had had the effect of standardizing the manufacture of automobiles, Mr. Reeves replied as follows:

"I don't think that is true, Senator. In every factory there was a fight on constantly to make changes, to make their car just a little bit better than somebody else's car and sell it at a low price if they could."

Mr. Edsel Ford, President of the Ford Motor Company, on examination by Mr. Hugh Cox of the Antitrust Division testified before the TNEC to the effect that his Company had followed the practice of taking out patents on inventions for the sole purpose of securing protection from infringement suits, that the Company had operated under a system of "mutual exchange" although not as a member of the Automobile Manufacturers Association, that the Company had followed the policy of granting licenses under its patents to all applicants, that its licenses had been granted on a royalty-free basis (except in one instance, in 1911), that the Company had not sued persons who had used its inventions without prior permission under a license (except in one instance, in 1909), that the Company had followed a policy of not paying royalties to inventors and had, instead, encouraged inventors by assisting them in getting into production and then

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purchasing products in which the inventions had been incorporated. (Hearings before the Temporary National Economic Committee, 75th Congress, Third Session, pursuant to Public Res. No. 113.)

The background of this position is also expressed in the recent book by the late Prof. Henry Simons of the University of Chicago. As you know, of course, Simons was one of the most respected thinkers in this field. His "A Positive Program for Laissez Faire" gave much comfort and ammunition to the critics of the New Deal, and Fortune has said his present book "will stand the test of time." In his chapter on "Postwar Economic Policy" which, incidentally, should be required reading in OMGUS, he lists four fundamental and minimal requirements, one of which is as follows:

> "Preparation and execution...of effective antimonopoly policies, involving systematic industrial deconcentration, dissolution of giant corporations and cartels, and effective prohibition of private monopolistic restraints of enterprise and trade."

To the attainment of that goal he devoted many pages of constructive thought which will undoubtedly have effect on political thinking and governmental policy at home. For instance, one sees there the first germ of the Marshall Plan. It is difficult to single out some from the many worthwhile passages but these few emphasize the point we are trying to make:

> "Deconcentration need involve little or no dismemberment of productional or operating units...selling must be divorced from manufacture; and industrial research must largely be dissociated from particular operating firms...Just as free trade requires free and equal access to markets, it likewise requires equal and reasonable access, if not wholly free access, to technical knowledge and patentable devices... when the facts about patent-pooling and about world cartels are more generally known, the argument for great corporations, in terms of contribution to research and technical progress, should turn and overwhelm those who have employed it...The role of international cartel syndicalism in the pre-war period is only beginning to be recognized clearly, as is the prospect that, failing wise measures of prevention, the old cartels will re-establish themselves promptly when hostilities cease...much will doubtless be accomplished under recent Supreme Court decisions in opening up patents by antitrust litigation. Reform in patent law and administration should be undertaken here and on a wide international front..."

But far more important than the words of leading thinkers in this field is the clearly announced policy of our Government. In addition to the policy of the Department of Justice in the Shoe Machinery case we have what amounts to an order from the President of the United States,

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transmitted by the Secretary of State to the Secretary of War, and by him to OMGUS. By that I should think we must be bound.

On 1 August 1946, Dean Acheson, the Acting Secretary of State, submitted a memorandum to the President of the United States on the subject, "Recommendations with Respect to German Domestic and Foreign Patents," and enclosed a document dated 10 July 1946 containing recommendations of the President's Executive Committee on Economic Foreign Policy. The recommendations called for the immediate establishment of a German patent office and provided with general respect to German patents, in part, as follows:

"(1) Any patent now in effect or hereafter granted shall be licensed to all applicants whether or not nationals of Germany, on a non-restrictive and non-discriminatory basis at a reasonable royalty and for the life of the patent.

"(2) In no case shall delays in the issuance of licenses be permitted to interfere with such production, use, rate or importation as the occupation authorities may deem desirable.

"(3) Existing provisions of German statutes, supplemented if necessary, requiring disclosure of sufficient information to render the invention claimed in the patent capable of practical exploitation shall be strictly enforced. Initial absence of such disclosure or failure promptly to correct insufficiency of disclosure shall be ground for invalidation of the patent, provided, however, that technical information, whether or not protected by patents, shall not be published if the occupation authorities deem publication prejudicial to security.

"(4) The occupation authorities shall take such steps, including necessary revisions of the German patent laws, to prohibit permanently the German Patent Office from maintaining a class of secret patents except as ordered in specific cases for the benefit of the occupation authorities.

"(5) Rights in patents and patent contracts and rights to the issuance of patents shall be subject to such blocking, impounding, security and other measures as the Allied authorities may prescribe. Such measures may include dedication to the public by termination, if it is decided that such termination will further any program which may be adopted by the occupation authorities concerning the disestablishment of combines, cartels or other prohibited

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arrangements. (Emphasis added.)

The President, in writing, approved these recommendations on 17 September 1946. The documents were transmitted by the Acting Secretary of State to the Secretary of War with the suggestion that they be forwarded to the Military Governor for action. By memorandum of 24 September 1946 the Civil Affairs Division of the War Department transmitted the documents to the Military Governor with the following statement:

> "Accordingly it is requested that you take such action as lies within your competence in implementation of these recommendations."

We note particularly the recommendation (to the President and approved by him) that measures in regard to patents, within a program concerning the disestablishment of combines, cartels or other prohibited arrangements, may include dedication. We have seen no order, statement, directive or request countermanding the recommendations which the President approved and which were transmitted by the War Department with a request for action. We can only conclude that dedication, and, a fortiori, measures short of dedication, are not only permissible decartelization actions in proper cases, but, indeed, are directed in such cases by the highest possible authority.

In specific relation to the Bosch situation, I should report that on Saturday I had a lengthy discussion with former General Wilson who is here representing Bosch. While we agreed in the beginning of our discussion that we were merely exploring the matter and that neither of us would be bound by any statements made, I am at liberty to report the result of our talk even though General Wilson is free under our agreement to change his position after talking with Bosch.

First I explained our situation. I said that if we found Bosch to be excessive under the Law I assumed we would separate therefrom several competing companies. There would be no question, I thought, about giving these divested units for future use such current Bosch assets as buildings, machinery, and so on. But what, I asked, would he do about the Bosch research laboratory which obviously could not be separated into parts for each new competitor. General Wilson said he thought the only thing to do was to give the new competitors free access to Bosch inventions for five or ten years. I asked him if he thought he could persuade Bosch to voluntarily agree to that for a period not to exceed five years. He said he would see them on Monday and Tuesday (23 and 24 February) in Stuttgart, would try to sell them on that suggestion, and would let me know by letter. Consequently, I do not think we can afford to take a position here, even if we disregard all the precedent and policy enunciated by our Government as shown above, which may turn out to be less inclusive than Bosch is prepared to give us voluntarily.

If we are not to require royalty-free licensing for five years then

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I think it would be unwise to announce that policy at least until we hear from General Wilson.

JOHNSTON AVERY

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